Editor's note: Appealed -- rev'd, remanded, Civ.No. 88-F-1748 (D. Colo. Nov. 9, 1989)

CYPRUS WESTERN COAL CO.

IBLA 86-119 Decided July 26, 1988

Appeal from a decision of the Director, Minerals Management Service, affirming an order requiring payment of advance royalties under Federal coal lease No. C-0128433. 83-0010-MIN.

Affirmed.

1. Coal Leases and Permits: Generally -- Coal Leases and Permits: Leases

Advance royalty provisions in a lease issued in 1975 under the Department's short-term coal leasing criteria were not modified by regulations promulgated in 1976 implementing the Federal Coal Leasing Amendments Act that governed the imposition of advance royalties. Where the lease made explicit provisions for how and when advance royalties were to be paid, and nothing in the regulations indicated an intent to modify the express lease terms, the lease terms were unaffected by promulgation of the regulations.

APPEARANCES: Michael S. McCarthy, Esq., Michael J. Cook, Esq., and Brian D. Wylie, Esq., Denver, Colorado, for appellant; William R. Murray, Esq., Office of the Solicitor, Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE KELLY

Cyprus Western Coal Company (Cyprus) appeals from a September 13, 1985, decision of the Director, Minerals Management Service (MMS). 1/ The Director affirmed a May 25, 1983, order of the MMS Royalty Management Program requiring Cyprus to make advance royalty payments under Federal coal lease No. C-0128433 commencing on June 1, 1980. The lease is located in secs. 19 and 30 of T. 5 N., R. 86 W., sixth principal meridian, in Routt County, Colorado. It was issued on June 1, 1975, by the Bureau of Land Management (BLM) to Morgan Coal Company, which immediately assigned the lease to Energy Fuels Corporation, a predecessor-in-interest of Cyprus.

1/ Cyprus is the successor in interest by merger to Colorado Yampa Coal Company and Getty Minerals Marketing, Inc., the appellants in the appeal to the Director, MMS.

The lease in question was issued under the short-term coal leasing criteria approved by then Secretary of the Interior, Rogers C. B. Morton, on February 13, 1973. These criteria permitted coal leasing only when:

> (a) the coal is needed to maintain an existing mining operation, or
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> (b) coal is needed as a reserve for production in the near future; and, in all cases
>
> (c) the land to be mined will be reclaimed in accordance with lease stipulations that will provide for environmental protection and land reclamation, and
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> (d) where required by the National Environmental Policy Act, an environmental impact statement covering the proposed lease has been prepared.

(Memorandum of Feb. 8, 1975, from Acting Assistant Secretary-Public Land Management to Secretary).

A June 6, 1975, memorandum from the Assistant Secretary to the Under Secretary recommended that issuance of the lease effective June 1, 1975, be approved. In recommending lease issuance, the Assistant Secretary also recommended that a number of stipulations be made a part of the lease, including one requiring advance royalty payments. This was incorporated into the lease as section 6(a) and states:

> Sec. 6. Advance Royalty. (a) An advance royalty shall be due monthly at the rate set forth in subsection 5(a) based upon the following annual production rates: 10,100 Tons per lease Month for the sixth Lease Year; 15,200 Tons per Lease Month for the seventh Lease Year; 20,200 Tons per Lease Month for the eighth Lease Year; 25,300 Tons per Lease Month for the ninth Lease Year; and 30,300 Tons per Lease Month for the tenth and each succeeding Lease Year.

Soon after the lease was transferred to Energy Fuels, the company began surface coal mining operations. The Director's decision reports that by October 1976, the lessee "had mined out the surface reserves in the Fish Creek coal seam and paid royalties of approximately $ 770,670 on 904,000 tons of coal produced from the lease" (Director's Decision at 1). No further mining activity has occurred on the lease since completion of the surface mining operation. Appellant does indicate that in "late 1979" it submitted a mine plan that made reference to the potential for underground coal mining on the lease (Appellant's Statement of Reasons (SOR) at 7-8).

Pursuant to section 6 of the lease, the Geological Survey 2/ notified appellant in a letter dated April 28, 1980, that advance royalty would be

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2/ By Secretarial order No. 3071, dated Jan. 19, 1982, as amended May 10, 1982, all minerals management functions previously exercised by the Conservation Division, Geological Survey, were transferred to MMS.

due and payable beginning with the sixth lease year commencing June 1, 1980. Appellant explains in its SOR that

> [w]hen Energy Fuels received the notice concerning advance royalties in April 1980, it was not prepared, either financially or technically, to confront the substantial difficulties involved with attempting to mine underground coal on the lease. In addition, Energy Fuels believed that the prospect for commercial recovery of the Wadge [underground coal seam] was highly uncertain and would involve several years of preparatory and developmental work.

(SOR at 11). Concluding it "had no option," Energy Fuels "tendered an offer to relinquish the lease" on June 1, 1980. This offer was subsequently withdrawn on December 9, 1981, before any action thereon had been taken by the Department. 3/

In a letter dated February 2, 1982, appellant requested that BLM issue a determination of appellant's rights and obligations under the lease. Appellant took the position that Federal coal management regulations issued in 1976 4/ had "superseded and rendered ineffective the advance royalty provisions of section 6 of the lease" (SOR at 12). Appellant's request was referred by MMS to the Department's Regional Solicitor's Office, Rocky Mountain Region, for an opinion on whether appellant was obligated under the lease to pay advance royalties. The Regional Solicitor's opinion, which is discussed infra in further detail, concluded that appellant was required to pay advance royalties as "the advance royalty provision can be viewed as part of a negotiated contract tailored to meeting both the Department's concerns and the needs of the lessee" (Regional Solicitor's Opinion of July 27, 1982, at 6). The opinion also found that regulations promulgated soon after the lease had issued had not released appellant from liability under section 6 of the lease. Id.

Pursuant to the conclusions in the Regional Solicitor's opinion, MMS issued its May 27, 1983, decision directing appellant to pay advance royalty in the amount of $ 724,826 for the period from June 1, 1980, through December 31, 1982. 5/ This decision was subsequently affirmed in the Director's decision of September 13, 1985, from which appellant has filed the instant appeal.

3/ The reason given for the withdrawal was that the stock of Energy Fuels was purchased in July 1981 by Getty Coal Company, which changed the name Energy Fuels to Colorado Yampa Coal Company.
4/ These regulations, found at 41 FR 56645 (Dec. 29, 1976) are discussed in further detail, infra.
5/ In the appeal before the Director, MMS, appellant contested the method used to calculate the advance royalty. This issue has not been raised in the present appeal.

Before considering the arguments made by appellant on appeal, we first note that certain events have occurred during the pendency of this appeal and the prior appeal to the Director which may serve to limit appellant's liability under section 6 of the lease. On June 30, 1983, appellant elected pursuant to the provisions of 30 CFR 211.20(b)(1) (now 43 CFR 3483.1(b)(1)) to subject the lease to the rules of 30 CFR Part 211 (now 43 CFR Part 3480). Regulation 30 CFR 211.20(b)(1), promulgated on July 30, 1982, 47 FR 33187, provides:

> Federal coal leases issued prior to August 4, 1976, until the first readjustment of the lease after August 4, 1976 shall be subject to the Federal lease terms, including those that describe the minimum production requirements, except that: (1) An operator/lessee holding such a lease may elect to be subject to the rules of [43 CFR Part 3480] by notifying the authorized officer in writing prior to August 30, 1983.

In considering whether appellant's election under 30 CFR 211.20 would limit appellant's liability, the Director quoted part of a March 29, 1985, memorandum received from the Colorado State Office, BLM, which stated:

> Amendments to the BLM regulations have not operated to nullify the obligation to pay advance royalty under Section 6 of the lease. Section 6 as well as other terms of the lease are subject to readjustment on June 1, 1995. Regulatory provisions which could affect Section 6 of this lease before June 1, 1995, are an approval of an LMU [Logical Mining Unit] which includes this lease or the acceptance of an election under 30 CFR 211.20. However, the approval of the first and/or the acceptance of the second would not apply retroactively to the date when advance royalty became due. [Emphasis added.]

(Director's Decision at 8).

The Director stated that appellant's election under 30 CFR 211.20 was still pending before BLM, and if approved, would become retroactive to April 1, 1983. 6/ The Director also stated: "[W]e accept BLM's determination that the regulation had no effect on Appellant's duty to pay advance royalty under section 6 of the lease prior to the effective date of the release." Id. at 9.

We now consider the arguments raised by appellant. Appellant makes two arguments in contending that it is not obligated under the lease to pay advance royalties. Appellant first argues that regulations setting advance royalty guidelines promulgated after the issuance of the lease in question superseded the advance royalty provision in the lease. Appellant claims that under the regulations, it would not be liable for advance royalty payments until June 1, 2005. In its second argument, appellant asserts that the advance royalty provision in the lease was never intended to be applicable to underground coal reserves.

6/ Regulation 43 CFR 3483.1(b)(1)(ii) states that the effective date of the election "shall be the most recent royalty reporting period prior to the submittal of the election to the authorized officer."

To fully review appellant's first argument requires an initial overview of the many statutory and regulatory changes that have been made to the Federal coal leasing system over the past several years. Section 7 of the Mineral Leasing Act of 1920 (MLA), 41 Stat. 439, as originally enacted required the "diligent development" of coal leases on Federal lands, but it was not until May 28, 1976, 1 year after issuance of appellant's lease, that the Department defined the term. 41 FR 21780. See H.R. Rep. No. 681, 94th Cong., reprinted in 1976 U.S. Code Cong. & Ad. News 1943, 1948-49. This definition was part of the Department's comprehensive program, initiated by Secretary Morton's February 18, 1973, approval of the memorandum previously discussed, to improve Federal coal leasing to meet concerns that lease lands were not being adequately developed and environmentally protected. Responding to these same concerns, Congress on August 4, 1976, enacted the Federal Coal Leasing Amendments Act (FCLAA), P.L. 94-377, 90 Stat. 1086 (1976). With respect to diligence requirements, Congress included provisions requiring that "[a]ny lease which is not producing in commercial quantities at the end of ten years [of the date of passage of FCLAA] shall be terminated." 30 U.S.C. § 207(a) (1982). FCLAA also made provisions for the payment of advance royalties in lieu of continued operations upon a determination by the Secretary that "the public interest would be served thereby." 30 U.S.C. § 207(b) (1982).

Soon after the passage of FCLAA, the Department promulgated amendments to the regulations defining and providing for advance royalty payments on Federal coal leases. Diligent development for leases issued before August 4, 1976 (the date of enactment of FCLAA) was defined to mean "the timely preparation for and initiation of production of coal from the LMU [logical mining unit] [7/] so that coal is actually produced in commercial quantities [8/] before June 1, 1986." 41 FR 56645 (Dec. 29, 1976); 43 CFR 3500.0-5(f)(2) (1977). In 43 CFR 3503.3-2(b)(1) (1977), the Department set forth the circumstances in which advance royalties would be imposed:

> § 3503.3-2 General statement on royalties.
> * * * * * *
> (b) * * *
> (1) The Mining Supervisor shall have discretion, upon the request of the lessee, to authorize the payment of an advance

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7/ The present definition for logical mining unit is found at 43 CFR 3480.0-5(a)(19), which provides:

"(19) Logical mining unit (LMU) means an area of land in which the recoverable coal reserves can be developed in an efficient, economical, and orderly manner as a unit with due regard to conservation of recoverable coal reserves and other resources. An LMU may consist of one or more Federal leases and may include intervening or adjacent lands in which the United States does not own the coal. All lands in an LMU shall be under the effective control of a single operator/lessee, be able to be developed and operated as a single operation, and be contiguous."

8/ 43 CFR 3480.0-5(a)(6) defines commercial quantities as "1 percent of the recoverable coal reserves or LMU recoverable coal reserves [the sum of estimated Federal and non-Federal recoverable coal reserves in the LMU (43 CFR 3480.0-5(a)(20))]."

> royalty in lieu of continued operation for any particular year. The advance royalty for each lease shall be based on a percent of the value of a minimum number of tons of coal, and the percent shall not be less than the percent prescribed in that lease for the production of royalty. * * * [F]or any lease issued before August 4, 1976, the minimum number of tons shall be determined on a schedule sufficient to exhaust the leased reserves in 40 years from June 1, 1976. Advance royalties shall not be paid for more than ten years in all during the life of any lease, including the life of the lease after readjustment. No payment of an advance royalty during the first 20 years of a lease may be used as a credit against production royalty due after the 20th year of that lease. The Mining Supervisor may, upon notifying the lessee six months in advance, cease to accept advance royalties in lieu of the requirement of continued operation.

This regulation shows that the Department in its rulemaking made payment of advance royalties, upon proper authorization, an alternative to meeting continued operation requirements in a lease year.

At this point we can consider appellant's arguments that the regulations promulgated in 1976 pursuant to FCLAA superseded and replaced the advance royalty requirement of section 6(a) of the lease. As pointed out in the Regional Solicitor's opinion, there is no requirement in the lease that the lessee be in production before the sixth lease year. Unlike the regulations promulgated in 1976, which permitted, upon authorization, payment of advance royalty in lieu of meeting continued production requirements, the provisions in section 6 made no such distinction. Commencing June 1, 1980, unless production levels were at or above the levels set in section 6(a), the lessee was required to make advance royalty payments. Thus, advance royalty payments could be required under the lease regardless of whether continued production had been met on the lease. Appellant argues that the advance royalty provisions originally set forth in the lease have been superseded and replaced "by the subsequent promulgation of inconsistent and overriding regulations" (SOR at 15). Appellant contends that this result is mandated by a clause set forth in the introduction of the lease. This clause states in relevant part:

> This lease [is] entered into on June 1, 1975 * * * pursuant and subject to the terms and provisions of the Act of February 25, 1920, 41 Stat. 437 as amended, 30 U.S.C. §§ 181-263 and to all regulations (including but not limited to, 30 C.F.R. P 211 and 43 C.F.R. Parts 23 and 3500) of the Secretary of the Interior <u>now or hereafter in force which are made a part hereof</u> * * *. [Emphasis added.]

Appellant argues: "The 'or hereafter' clause becomes dispositive in this appeal because the Department promulgated successive generations of Federal coal leasing regulations following Lease issuance, all of which spoke directly to the payment of advance royalties" (SOR at 17). Appellant claims the later regulations have been made a part of the lease through the function of the "hereafter" clause, and, because the subsequent regulations are "different" than the lease provisions, the rule requiring payment of advance royalties

only as in lieu payment for continued production must govern. Accordingly, we must consider whether the clause quoted above can be viewed as incorporating the regulations in a manner that absolves appellant from paying advance royalties under section 6 of the lease.

[1] Contrary to appellant's assertions, we fail to recognize any intent on the part of the Department to supersede the express terms of appellant's lease. As correctly pointed out in the MMS answer, the clause in the lease relied upon by appellant

> must be read in light of the discretion reserved by the Secretary in various lease provisions and by matters not specifically addressed in the lease, such as reclamation standards and bonding. Regulations "hereafter in force" thus refers to rules which provide procedures, which implement reserved discretion or which provide explicit standards and definitions for undefined terms in the lease.

(MMS Answer at 11).

Indeed, this Board has essentially so interpreted this clause in a number of appeals challenging coal lease readjustment terms. Thus, in Lone Star Steel Co., 77 IBLA 96 (1983), the appellant objected to this language on the ground that the provision required the company to agree in advance to "presently unknown terms embodied in future regulations." Id. While the Board ultimately overruled the appellant's objections, it was careful to point out that "[i]t is noteworthy that there is a statutory restraint against the readjustment of the basic lease terms except at the intervals specified." Id. at 98 n.2, citing Rosebud Coal Sales Co. v. Andrus, 644 F.2d 849 (10th Cir. 1982). See also Ark Land Co., 97 IBLA 241 (1987).

If we were to adopt appellant's position, we would in essence be permitting the unfettered readjustment of specific lease terms. Provisions permitting lease readjustment only every 20 years would be rendered meaningless. Further, while appellant's construction might work in its favor in this instance, one can perceive instances when such a construction would work to the lessee's detriment. Had, for example, the Department implemented diligent development requirements more stringent than those found in the lease, appellant's interpretation of the "hereinafter" clause would have placed it under standards more onerous than those agreed upon in the lease. Thus we must conclude that the subsequently adopted regulations did not effect and could not have effected a modification of any basic lease term in outstanding leases.

We now turn to appellant's second contention against imposition of the advance royalty requirement. Appellant states that it has "consistently maintained that the advance royalty provisions of the lease were never intended to apply to underground coal reserves" (SOR at 27). Appellant asserts that the lease "when read as a whole, is clear on this point." Id.

Appellant concedes that the lease as issued included both the surface and underground reserves, and further acknowledges that section 6, when read alone, does not distinguish between the two types of reserves or indicate that its provisions were to be applicable to only one type of reserve. It contends,

however, that when section 6 is read in conjunction with two other provisions in the lease, sections 8 and 11, it becomes clear that advance royalty provisions were applicable only to the surface coal reserves. To review this argument, we first consider the purpose and content of these sections of the lease.

Sections 8 and 11 of the lease provide in relevant part:

> Sec. 8. Minimum Production. The Lessee shall produce Coal from the leased lands in accordance with the mining plan required by Section 11 of this Lease, * * *.
> * * * * * * *
>
> Sec. 11. Mining Plan. (a) The Lessee shall file in sextuplicate with the Mining Supervisor on or before the third Anniversary Date a detailed development, production and reclamation plan in accordance with the provisions of 30 C.F.R. Part 211 and 43 C.F.R. Part 23. The plan is referred to in this Lease as the "mining plan." The plan shall include: (1) a schedule of further planning and exploratory operations, the development, production, processing, and reclamation operations and other activities to be conducted under this Lease; * * * and (3) a showing that the Lessee will use all due diligence (A) to extract all Coal in the Leased Lands which can be safely recovered by approved mining methods consistent with the protection and use of other natural resources and with sound economic practice and (B) to attain production from the Leased Lands at a rate at least equal to the rate on which advance royalty for this Lease is computed.

Appellant relies on the language in section 11 that states that the mining plan required under this section had to provide a "detailed development, production and reclamation plan" and had to include a schedule of future "development and production" under the lease. More importantly, appellant asserts, "the mine plan had to demonstrate that [appellant] intended to extract 'all coal which can be safely recovered by approved mining methods' in order to obtain production at a rate at least equal to the advance royalty rate provided for in the lease" (SOR at 34). Thus, appellant asserts that "[i]f the advance royalty provisions contained in section 6 were intended to apply to the underground reserves, sections 8 and 11 of the Lease required that [appellant's] approved mine plan describe [underground mining] operations in considerable detail." Id. Because appellant's mine plan was approved with "no reference whatsoever" to an underground operation soon after the lease was issued, appellant concludes that this approval is an indication the lease only required development of the surface reserves.

While appellant has not explicitly so stated, it apparently is arguing here that since its mine plan made no mention of underground reserves, the approval of that plan modified the plain language of section 6 requiring payment of advance royalty when production does not meet lease standards. We can read no such intent to modify either into the mine plan provisions of section 11 or in the approval of the plan submitted by appellant. While it is true section 11 speaks in terms of developing a plan for "all coal," there is nothing in this or other sections of the lease to indicate that

approval of an initial mining plan excused appellant from its obligations regarding coal leased to appellant but not contemplated in the mining plan. To the contrary, it appears that pursuant to section 25 of the lease, appellant's breach of the provisions of section 11 was waived. Section 25 states that the United States "reserves the right to waive any breach of the conditions contained in this Lease, except the breach of such conditions as are required by the [Mineral Leasing] Act." By approving the mining plan as submitted by appellant, the Department in essence waived appellant's failure to include mining information on the underground reserves.

In arguing that the advance royalty provisions of the lease were never intended to apply to underground reserves, appellant next contends that certain acts and failures to act on the part of the parties before, during, and after the execution of the lease "show that the underground reserves were not to be considered for advance royalty purposes" (SOR at 27). In other words, appellant seeks to go outside the lease document to show it does not owe advance royalties.

In particular, appellant points to various letters written during lease negotiations which, according to appellant, "make it explicitly clear that it had no immediate or future plans to develop the underground coal reserves included in the lease." Id. For example, the president of Energy Fuels stated in a May 7, 1974, letter to BLM:

> Energy's present and future mining plans are based on stripping overburden to recover all of the strippable coal in the Fish Creek, Lennox and Wadge seams underlying the areas shown on the map attached as Table 1. All of the coal in the shallow Fish Creek seam is located within 50 feet from the surface and will be recoverable from the Fish Creek Pit shown on Table 1 and Table 2. The deeper Lennox and Wadge seams will be stripped to depths ranging from 60 to 120 feet from the surface and will be recovered from the Wadge Pit shown on Table 1.
>
> The combined Fish Creek, Lennox and Wadge seam coals will be sufficient to sustain the production increases scheduled for the next three years to reach an annual rate of 4,000,000 tons during the year ending March 31, 1978, at which time production is expected to stabilize at that rate over the remaining life of the strippable reserves. Exhibit 14, pp. 3-4. [Emphasis supplied by appellant.]

(SOR at 29). See Appellant's Exhibit 14. In addition to the letters, appellant cites to the prelease environmental assessment reports, the prelease mine plan, and the Under Secretary's recommendations set forth in a memorandum dated June 6, 1975. In this memorandum, the Department notes that mining would be by strip mining.

From these documents it is clear that at the time the lease was issued, the parties did not contemplate any immediately foreseeable mining of the underground reserves. However, we have carefully reviewed all of the documentation cited by appellant and fail to find any intent to lease only the surface reserves. With the ratification of the lease, all deposits of coal, surface

and underground, were included, as appellant has acknowledged. Nowhere in this correspondence is the intent expressed by either party to exclude the underground reserves from the lease.

In fact, if we were to find that the original parties had intended to exclude the underground reserves from the advance royalty provisions of section 6, as appellant contends, we would be forced further to find that the underground reserves had never been leased to the original lessee. This is true because section 6, which contains no language qualifying its applicability to leased coal reserves, necessarily applies to all leased reserves, and, as we previously found, no other provision in the lease limits the applicability of section 6. Thus, if we were to accept appellant's extrinsic evidence arguments, we would be required further to find that the lease is no longer in existence, since all of the surface reserves have long since been depleted. 9/

Our review of the issues and arguments raised by appellant has failed to show error in the MMS decision requiring payment of advance royalties.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

John H. Kelly
Administrative Judge

We concur:

Wm. Philip Horton
Chief Administrative Judge

James L. Burski
Administrative Judge

9/ Even if appellant were correct that the section 6 "Advance Royalty," applied only to coal removed by surface mining methods, appellant would still be required to tender advance royalty. Nothing in any part of the lease, be it section 6 or section 11, makes payment of advance royalties contingent upon the existence of mineable reserves. Advance royalty payments are required for every month commencing in the sixth year regardless of whether or not production is occurring, has occurred, or will ever occur, and this obligation continues so long as the lease remains in effect. In order words, the obligation to tender advance royalties is absolutely independent from any production aspect of the lease. If section 6 were limited to coal removed by surface mining the only effect would be that, under section 7 of the lease, the advance royalties required under section 6 could only be applied to future surface coal production. Thus, if we accepted appellant's interpretation, it would still be liable for advance royalty but could only apply such payments to future surface production, which would make such payments a total loss since appellant has already mined all coal amenable to surface mining techniques.